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FISCAL IMPACT STATEMENT

LS 7194

BILL NUMBER: HB 1724

NOTE PREPARED: Feb 15, 2005

BILL AMENDED: Feb 14, 2005

SUBJECT: Agriculture.

FIRST AUTHOR: Rep. Buck

FIRST SPONSOR:

BILL STATUS: CR Adopted - 1st House

FUNDS AFFECTED: X GENERAL
X DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: (Amended) The bill permits the Enterprise Zone Board to designate certain areas as Agricultural Enterprise Zones. The bill provides exemptions from property taxes and the Adjusted Gross Income Tax for agricultural processing facilities located in the Zones. The bill provides that real and personal property located in a Zone may be assessed for payment of property taxes committed to funding or paying bonded indebtedness or certain lease rentals.

Effective Date: July 1, 2005.

Explanation of State Expenditures: (Revised) *Agricultural Enterprise Zones (AEZs):* The Indiana Economic Development Corporation (IEDC) would incur additional administrative expenses relating to application review, designation, and administration of Agricultural Enterprise Zones (AEZs) by the IEDC Board. Under HEA 1003-05, the State Enterprise Zone Board has been abolished and its responsibilities have been transferred to the IEDC and IEDC Board. Under the bill, the IEDC Board would have to contract with a state university for annual evaluations of the AEZs. Under current statute, funding for expenses relating to the administration of the EZ program is derived from the registration fee charged to EZ businesses that receive tax incentives. The registration fee is 1% of the tax incentive benefits exceeding \$1,000 received by an EZ business. The registration was not changed by HEA 1003-05. The bill, however, excludes tax incentive recipients in AEZs from this registration fee. (Note: The bill also excludes incentive recipients in AEZs from paying the participation fees imposed by Urban Enterprise Associations (UEAs) on EZ businesses.) The IEDC should be able to implement the AEZ program under current staffing and resource levels.

Background: The bill would authorize the IEDC Board to designate up to 10 AEZs within municipalities containing an Urban Enterprise Zone (EZ) with a Urban Enterprise Association (UEA). (Note: Currently, there

are 25 municipal EZS.) The bill limits the designation period to CY 2006. The AEZs may operate for up to 15 years. The bill authorizes a municipal executive to apply to the IEDC Board for designation of an AEZ upon approval by resolution of the municipal legislative body. Under the bill, the IEDC Board must evaluate the application if the proposed AEZ meets the following threshold criteria:

- (1) At least 25% of the households in the AEZ are below the poverty level.
- (2) The proposed AEZ is entirely within the applicant municipality and is suitable for the development of at least one agricultural processing facility.
- (3) A UEA for an EZ in the municipality has been appointed.

Under the bill, IEDC Board would have to evaluate the application for an AEZ that meets the threshold criteria, and either designate the AEZ or reject the AEZ application based on the following factors:

- (1) The level of poverty, unemployment, and general distress of the area in comparison with other applicant and non-applicant municipalities, and the expression of need for an AEZ.
- (2) Evidence of support for designation by residents, businesses, and private organizations in the proposed AEZ and the demonstration of a willingness among AEZ constituents to participate in revitalization of the area.
- (3) Efforts by the applicant municipality to reduce the impediments to development in the AEZ, including: streamlining local government regulations and permit procedures; crime prevention activities involving AEZ residents; and a plan for infrastructure improvements capable of supporting increased development activity.
- (4) Significant efforts to encourage the reuse of existing AEZ structures in new development activities to preserve the existing character of the neighborhood, where appropriate.
- (5) The capacity of the UEA to carry out the goals and purposes of the EZ and AEZ laws.

The bill requires an AEZ business to annually report various employment, wage, investment, and other business activity information to the IEDC Board. The bill also requires such businesses to submit to the IEDC Board income tax returns, assessment records, personal property tax returns, and other supporting documentation requested by the IEDC Board. The bill also requires the IEDC Board to contract with a state university to prepare an annual evaluation of the economic effects of AEZs to the Legislative Council.

Explanation of State Revenues: *AEZ Income Tax Exemption:* The bill establishes an Adjusted Gross Income (AGI) Tax exemption for individual and corporate taxpayers that operate an agricultural processing facility in an AEZ and meet certain investment and employment criteria. The exemption would extend to income derived by the taxpayer from sources inside an AEZ. These sources would be income from real or tangible personal property located in an AEZ; (2) income from doing business from an agricultural processing facility in an AEZ; or (3) income from intangible personal property with a situs in an AEZ. The bill prohibits a single taxpayer from receiving more than \$10.0 M in tax reductions from the AGI Tax exemption and the property tax exemption also established by this bill (see below under *Explanation of Local Revenues*).

The net revenue impact of the AGI Tax exemption is contingent on the scope of the AEZs that are designated. It also depends on the extent that collections from taxable activities and earnings attributable to the investment

in new property or new employees is less than or exceeds the amount of the exemption claimed by AEZ businesses. However, if the investment or new employment would have occurred in the absence of the tax exemption, the net impact would be the AGI Tax that would otherwise be collected on the exempt income. Contingent on the AEZ designations that occur in 2006, the fiscal impact could potentially begin in FY 2008 and end in FY 2022.

To qualify for the exemption, the taxpayer must operate an “agricultural processing facility” in an AEZ and either: (1) invest at least \$1.0 M in the facility and create at least five new jobs, in the case of a facility that relocates to the AEZ; or (2) increase the number of full-time employees working at the facility by at least 10% after the AEZ is designated, in the case of facility that was already located in the AEZ. The bill defines an “agricultural processing facility” as a building or complex of buildings (including the land it is situated on) that is used, or that is designed and constructed to be used, to: (1) transform agricultural products into goods that are used for intermediate or final consumption, including goods for nonfood use; or (2) package, sort, or grade agricultural products. The bill provides a methodology for the apportionment of income to the AEZ for taxpayers that are unable to separate income derived inside and outside an AEZ. The tax exemption expires when an AEZ’s designation expires. In addition, the tax exemption is phased-down during the last three years that the AEZ is designated as presented in the table below.

Phase-Down of AEZ Income Tax Exemption		
Two Years Before Final Year of AEZ Designation	One Year Before Final Year of AEZ Designation	Final Year of AEZ Designation
25% reduction	50% reduction	75% reduction

Businesses can be disqualified for the exemption for substantially reducing or ceasing an operation elsewhere in Indiana to relocate in an AEZ. In addition, the bill provides that a taxpayer claiming the exemption is ineligible for: (1) the EZ Inventory Tax Credit; (2) the EZ Employment Expense Credit; (3) the EZ Loan Interest Credit; (4) the EZ Investment Cost Credit; and (5) the Neighborhood Assistance Credit.

Revenue from the AGI Tax on corporations is deposited in the state General Fund. The revenue from the AGI Tax on individuals is deposited in the state General Fund (86%) and the Property Tax Replacement Fund (14%). The exemption is effective beginning in tax year 2007.

Explanation of Local Expenditures:

Explanation of Local Revenues: *AEZ Property Tax Exemption:* The bill would exempt agricultural processing facilities, and business personal property of these facilities, located in AEZ from property taxation if the taxpayer meets the investment and employment requirements also specified for the AGI Tax exemption (see above under *Explanation of State Revenues*). The exemption would be effective for 2007 Pay 2008 taxes. The exemption could potentially continue through 2021 given that AEZs are to be designated in 2006 and are limited to 15 years. However, property owners would not be exempt from property taxes resulting from local bonded indebtedness or lease rentals with an original term of at least five years. The bill would subject taxpayers obtaining the property tax exemption to the same limitations and the same phase-down provided for the AGI Tax exemption (see above under *Explanation of State Revenues*).

In general, the exemption would reduce the assessed value tax base in local taxing districts that contain AEZs.

This would cause a shift of the property tax burden from the taxpayers receiving the exemptions to all other taxpayers in those taxing districts. The actual fiscal impact depends on the amount of additional property that would qualify for the exemption under this proposal.

AEZ Income Tax Exemption: Because the proposed exemption, as it applies to individual filers who may operate an agricultural processing facility in an AEZ, would serve to decrease Taxable Income, counties containing AEZs and imposing local option income taxes (CAGIT, COIT, and/or CEDIT) may, as a result, experience an indeterminable decrease in revenue from these taxes. However, this impact could be diminished to the extent that new employment arises in AEZs due to the exemptions provided in this bill

State Agencies Affected: Indiana Economic Development Corporation; Department of State Revenue; Department of Local Government Finance.

Local Agencies Affected: Municipalities with Urban Enterprise Zones; counties with a local option income tax.

Information Sources:

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